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Supreme Court, U.
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IN THE

Supreme Court of the United States

No. 71-1700

SPERRY RAND CORPORATION,
Petitioner,
v.
A-T-O, INC., ELECTRONIC CONCEPTS, INC.,
JOHN E. ZENTMEYER, JR., and GUS K. TEBELL, JR.,
Respondents.

RESPONSE TO PETITION

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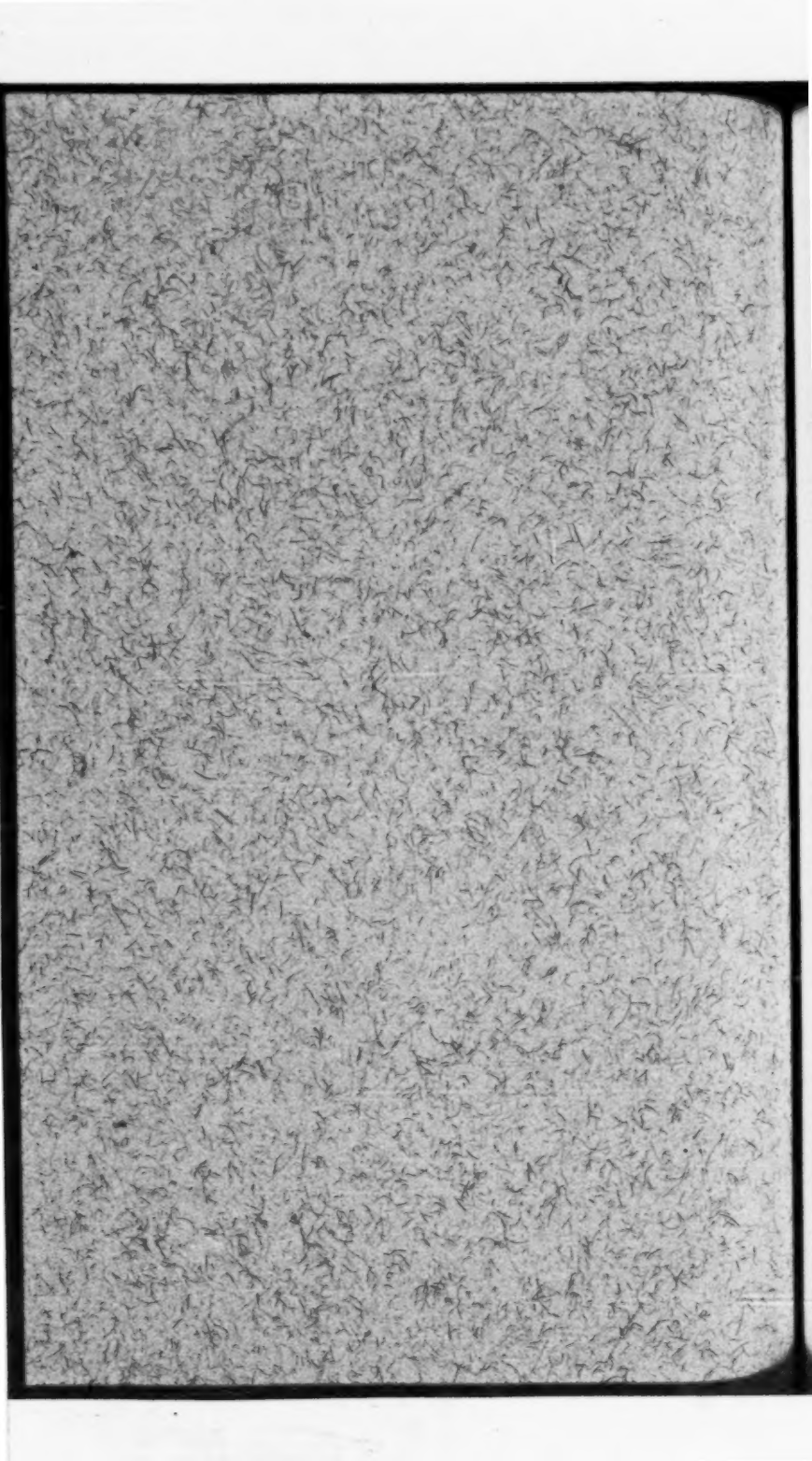

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BRIEF FOR RESPONDENTS

STATEMENT

On October 15, 1970, the United States District Court for the Eastern District of Virginia, having jurisdiction on the basis of diversity of the citizenship of the parties, 28 U.S.C.A. § 1332, held respondents liable for misappropriation of petitioner's trade secrets, granted injunctive relief, and awarded to petitioner $406,012 in compensatory damages, $185,000 in punitive damages, and $225,000 in attorney's fees, a total money judgment against respondents of $816,012, (Pet. App. A-21).

On September 7, 1971 the United States Court of Appeals issued its order on appeal, affirmed the findings of the District Court as not clearly erroneous, and approved certain of the awards, but reversed as to a duplication in compensatory damages in the amount of $175,000, and set aside the award of attorney fees as contrary to applicable Virginia law. The Circuit then remanded the

case to the District Court for the reassessment of damages in accordance with its opinion, (Pet. App. B-15, C-1), and cross-motions for rehearing were denied on April 11, 1972. A petition for certiorari to review that decision was filed in this Court on June 20, 1972 and is now pending (No. 71-1649).

QUESTIONS PRESENTED

I. Has this petition been previously denied on the merits?

II. Does the holding of the Fourth Circuit conflict with this Court's decision in *Guaranty Trust Co.* v. *York*?

III. Is there a conflict of decision between Circuit Courts of Appeals on the applicable rule?

IV. Is this the exceptional case which calls for the application of 'historic equity jurisdiction' to override state law denying attorneys fees?

ARGUMENT

I

This Application Is Duplicative

On February 4, 1972 during the pendency of the motions for rehearing before the Circuit Court, Sperry filed its petition in this Court on the same issue here presented. That application was denied on March 27, 1972, —— U.S. ——, 92 S.Ct. 1292.

It is not clear what purpose Sperry seeks to accomplish by substantially reprinting and refiling a previously denied petition where the question so re-presented has either been passed on by this Court or could have been raised, if open, by cross-petition in the then pending application in No. 71-1649. The response previously made to Sperry's

earlier petition addressed itself both to prematurity and to the merits now reargued.

The denial of certiorari by this Court was unqualified and although Sperry now assumes (Pet. 2) that such denial went solely to the question of prematurity, only the records of this Court can show whether the denial was both procedural and substantive or either.

In any event, to the extent that an aspect of the merits may remain open for further review beyond the issues presented to the Court in 71-1649, we repeat the response previously made to show the lack of substance in Sperry's petition.

II

Petitioner Shows No Conflict With The Decisions Of This Court

The conclusion of the Fourth Circuit "that Virginia would treat this case within the general rule denying counsel fees . . ." (Pet. B-12) remains uncontested in the petition. The only question raised is whether that Court improperly used Virginia law to reverse the fee award, instead of affirming the allowance in opposition to state law by using its 'historic equity jurisdiction.' As a first argument, the petition contends (Pet. 5) that the Circuit ruling conflicts with a principle announced by this Court in *Guaranty Trust Co.* v. *York*, 326 U.S. 99, 65 S.Ct. 1464 (1945), 160 ALR 1231.

The landmark opinion of Mr. Justice Brandeis in *Erie R. Co.* v. *Tompkins*, 304 U.S. 64, 58 S.Ct. 817 (1938), 114 ALR 1487, held that a federal general common law did not exist, and that federal courts should apply state precedents in diversity actions. Within a week of that decision, this rule was also applied to federal courts sitting in equity,

> The [*Erie*] doctrine applies though the question of construction arises not in an action at law, but in a suit in equity.
>
> *Ruhlin* v. *New York Life Insurance Co.*, 304 U.S. 202, 205, 58 S.Ct. 860, 861 (1938).

and must be applied even when changes in state law occur during appeal, *Huddleston* v. *Dwyer*, 322 U.S. 232, 64 S.Ct. 1015 (1944). As said in *Bernhardt* v. *Polygraphic Co. of Am.*, 350 U.S. 198, 202-203, 76 S.Ct. 273, 276 (1956),

> We deal here with a right to recover that owes its existence to one of the States, not to the United States. The federal court enforces the state-created right by rules of procedure which it has acquired from the Federal Government and which therefore are not identical with those of the state courts. Yet, in spite of that difference in procedure, the federal court enforcing a state created right in a diversity case is, as we said in *Guaranty Trust Co. of New York* v. *York* 326 U.S. 99, 108, 65 S.Ct. 1464, 1469, 89 L.Ed. 2079, in substance "only another court of the State." The federal court therefore may not "substantially affect the enforcement of the rights as governed by the State."

Supporting the holding of the court below, state law under the *Erie* rule was held to be a proper basis for denying counsel fees in both trade secret cases cited in the reprinted petition, *Aerosonic Corp.* v. *Trodyne Corp.*, 402 F. 2d 223 (5th Cir. 1968) and *Forest Laboratories, Inc.* v. *Pillsbury Co.*, 452 F. 2d 621 (7th Cir. 1971).

Despite this clear, and we believe unbroken, line of authority supporting the now questioned holding of the Fourth Circuit, petitioner argues nevertheless (Pet. 5) that a conflict exists between that holding and this Court's ruling in *Guaranty Trust Co.* v. *York*, 326 U.S. 99, 65 S.Ct. 1464 (1945), 160 ALR 1231. In respondents' opinion, petitioner misreads that decision. *Guaranty* is a

principal authority to the contrary and directly supports the reference to Virginia law by the Fourth Circuit. In *Guaranty* this Court said (p. 112),

> The source of substantive rights enforced by a federal court under diversity jurisdiction, it cannot be said too often, is the law of the States. Whenever that law is authoritatively declared by a State, whether its voice be the legislature or its highest court, such law ought to govern in litigation founded on that law, whether the forum of application is a State or a federal court and whether the remedies be sought at law or may be had in equity.

And the decision given was that a federal equity court sitting in a diversity action lacked power to apply the historic doctrine of laches to override the bar of a New York statute of limitations.

It is true that the variation in federal-state equity procedures was also noted in *Guaranty*, citing *Sprague* v. *Ticonic Bank*, 307 U.S. 161, 59 S.Ct. 777 (1939), but this Court emphasized in so doing that:

> Whatever contradiction or confusion may be produced by a medley of judicial phrases severed from their environment, the body of adjudications concerning equitable relief in diversity cases leaves no doubt that the federal courts enforced State-created substantive rights if the mode of proceeding and remedy were consonant with the traditional body of equitable remedies, practice and procedure, and in so doing they were enforcing rights created by the States and not arising under any inherent or statutory federal law. (326 U.S. 99, 106, 65 S.Ct. 1464, 1469)

The ruling of the Court below, which is here complained of, is not in conflict with *Guaranty Trust Co.* v. *York*, or any other decision of this Court given after the holding in *Erie* in 1938, and the question raised is neither open nor substantial.

III

There is No Conflict Between Circuit Courts On The Applicability Of State Law Under The *Erie* Rule To Determine A Claim Of Right To Counsel Fees In a Diversity Tort Suit

In support of the argument that counsel fees have been awarded in diversity cases in contradiction to local law provisions, the petition (p. 7) lists seven United States Circuit Court opinions asserted to be in conflict with the present ruling. A reading of these decisions shows the alleged conflict to be non-existent.

The petitioner takes as its starting point this Court's holding in *Sprague* v. *Ticonic National Bank*, *supra*. That citation sustained claims of beneficiaries to trust funds in the hands of a receiver of a national bank. As there stated, the claimant 'enforced the fiduciary obligation of the Ticonic Bank' and 'by establishing her claim necessarily established the claims of fourteen other trusts pertaining to the same bonds.' (307 U.S. 161, 166-167, 59 S.Ct. 777, 780). This Court held that under such circumstances the District Court could review the availability of the funds in the hands of the receiver, and in its discretion might reimburse plaintiff for costs of her counsel.

Sprague is not only not a diversity action, it differs in three other legally significant respects from the present case. It involved a federal receivership question on the extent of a statutory lien created under section 11(k) of the Federal Reserve Act, the breach of a fiduciary relationship, and the creation of rights in a fund from which fees could be paid.

Six of the seven citations from Circuit Courts listed in the petition do indeed follow the *Sprague* principle. Each of the six is a case where a party to a fiduciary relationship has created or protected a trust fund for the benefit of a class and fees are awarded as a lien on the fund. As

this Court said in *Mills* v. *Elec. Auto-Lite Co.*, 396 U.S. 375, 397, 90 S.Ct. 616, 628, (1970), such an award "conferred a substantial benefit on the members of an ascertainable class," and merely imposed on other *plaintiffs* a share in the costs they "would have had to pay . . . had it brought the suit."

The six cases and their holdings are as follows:

Cleveland v. *Second Nat. Bank & Trust Co.*, 149 F. 2d 466 (6th Cir. 1945) *cert. denied* 326 U.S. 775 (1945). Counsel fees of bank trustee are payable from protected trust fund.

First National Bank & Trust Co. of Racine v. *Village of Skokie*, 190 F. 2d 791 (7th Cir. 1951), *cert. denied* 342 U.S. 909 (1952). Charges of court appointed master and auditor are payable from sinking fund on sewer bonds. No counsel fees noted.

Mercantile-Commerce Bank & Trust Co. v. *Southeast Arkansas Levee Dist.*, 106 F. 2d 966 (8th Cir. 1939). Counsel fees of bank trustees are payable from protected trust fund.

Bank of China v. *Wells Fargo Bank & Union Trust Co.*, 209 F. 2d 467 (9th Cir. 1953). Counsel fees of bank stakeholder in interpleader payable out of funds in court registry.

Brisacher v. *Tracy-Collins Trust Co.*, 227 F. 2d 519 (10th Cir. 1960). Counsel fees of bank trustee payable from trust interest of complaining beneficiary.

Angoff v. *Goldfine*, 270 F. 2d 185 (1st Cir. 1959). Counsel fees payable from fund created in derivative stockholder action.

The seventh case, *National Van Lines* v. *Dean*, 237 F. 2d 688 (9th Cir. 1965) combined counts under federal and state trademark law. Counsel fees were approved although the federal question was not reached. However,

the same Circuit reached back ten years later, cited *National Van Lines* in reversing the interpretation on which it was based, and in a broad analysis which received particular commendation from this Court, reestablished the general rule against the allowance of attorney fees except under specific statutory or state authority, *Maier Brewing Co.* v. *Fleischmann Distilling Corp.*, 359 F. 2d 156 (9th Cir. 1966), *affd.*, 386 U.S. 714, 87 S.Ct. 1404 (1967).

In *Maier*, the Ninth Circuit dismissed the argument that *Sprague* v. *Ticonic Bank* was authority for the allowance of such fees, holding (p. 164, ftn. 13)

> Only one case has cited *Sprague* in a case comparable to the present one, *Carter Prods., Inc.* v. *Colgate-Palmolive Co.*, D.Md., 1963, 214 F. Supp. 383, and that was a patent case, where the statute does provide for the recovery of attorney's fees.

The reprinted petition further lists (pp. 8, 10) *Forest Laboratories, Inc.* v. *Pillsbury Co., supra*, a reversal of the award of attorneys fees by a District Court which had been cited to this Court as an authority in the prior petition *sub. nom. Forest Laboratories, Inc.* v. *Formulations, Inc.*, 320 F. Supp. 211, (E.D. Wis. 1970).

Petitioner also cites (Pet. 9) decisions in the fields of civil rights, patents, labor and other federal questions, some merely enforcing statutory allowances of fees, and other cases which consider the imposition of procedural court "costs." But, fees are not such costs and the state rule must be applied. Thus, citing *Erie* and *Guaranty*, this Court held that a New Jersey law requiring the giving of security for costs in a stockholder action, "goes beyond payment of what we know as 'costs' " and therefore, must be applied in such diversity suits in federal courts, *Cohen* v. *Beneficial Indusrial Loan Corp.*, 337 U.S. 541, 555, 69 S.Ct. 1221, 1230 (1949).

The rule established in *Erie*, and applied by the Court below to reference Virginia law on the disallowance of counsel fees in a diversity tort action, remains the applicable rule in all Circuits, and petitioner's suggested exceptions show no conflict of decision between them on the point.

IV

On The Affirmed Findings, This Is Not The Exceptional Case Claimed By Petitioner

To show the 'exceptional' character of this case, the petition argues that respondents "fraudulently . . . consume[d] the time of the court . . . with no justification," that there is "need of courts to control the behavior of litigants" and to make exceptions to the right of any defendant "to his day in court," particularly under the conditions of "today's overcrowded dockets" (Pet. 13). It is clear, therefore, that the gravamen of the petition's claim that this is an exceptional case lies in the implied assertion that any defense made by respondents to petitioner's charges constituted intransigent and contumacious behavior.

To reply to this argument, respondents must necessarily first concede that the District Court was of the opinion that the actions of respondents were 'calculated,' 'deliberate,' 'reprehensible,' 'misconduct' in 'blatant violation' of a duty of 'fidelity and loyalty to [Sperry]' (Pet. App. A), since the petition argument is based on a repetition of these characterizations—'theft' (Pet. 3), 'falsehood and fabrication,' 'malicious disregard for the rights of the plaintiff Sperry,' 'the stolen contract,' 'testified falsely' (Pet. 4), 'flagrant and deliberate,' 'false testimony', 'distortion and misrepresentation' (Pet. 12) etc.

It is the answer of respondents, that, without argument to this court on the truth or falsity of any statements of fact, the affirmed findings and concessions of

record alone show a more than adequate basis for the making of a defense in good faith to such charges. For brevity we cite only two illustrations.

1. The Coast Guard antenna design, held to be a trade secret of Sperry Rand, and for the misuse of which a principal amount of the various damage awards were assessed against respondents, was the work of the respondent engineer Zentmeyer, (Pet. A-7, B-4). He had been, two and a half years before the operative events held to constitute misuse, an employee of the petitioner, Sperry Rand, and had among his professional papers, after that employment, a copy of his design, (Pet. A-10).

While Zentmeyer was employed by Sperry, as the Circuit Court affirms, (Pet. B-4),

> Zentmeyer was so enthusiastic about fulfillment of the Coast Guard specifications and so confident that he had made new discoveries that he filed an invention description sheet with the Sperry Rand patent department. The patent department concluded, however, that because of disclosures in the prior art, the newly developed antenna array was not patentable.

The actual language of Sperry's patent department to Zentmeyer in the record on this was

> We have particular reference to [1952, non-Sperry] patent 2,730,717 which shows substantially the same antenna configuration. The invention appears to be taught completely . . . (Joint App. on Appeal, AE-17)

Nonetheless, it is this 'configuration' which was held to be the trade secret of petitioner, for the copying of which the respondents were held to have secured "an unjust and immoral advantage, of $175,000," (Pet. A-12).*

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* The legal question here raised under *Sears Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225, 84 S.Ct. 784 (1964), and *Compco Corp.* v. *Day-Brite Lighting, Inc.*, 376 U.S. 234, 84 S.Ct. 779 (1964), is a principal issue in No. 71-1649.

Respondents say that on the affirmed finding of this patent disclosure alone, their defending against petitioner's trade secret claim, if not conclusive, was clearly not without some reasonable basis in law.

2. The petition also argues exceptionality in that Sperry was "force[d] to take and retake vast amounts of testimony before and during the trial until, bit by bit, the true facts were brought to light." (Pet. 12). Respondents answer that Sperry, as plaintiff, necessarily made the going, and the costs it now complains of were largely incurred through its own abuse of the liberality of the Federal Rules of Civil Procedure.

For example, the Sperry complaint claimed

> RADAR, LORAN and related navigational and marine equipment and associated systems, all of which constitute and have constituted plaintiff's trade secrets. (Joint App. on Appeal, p. 10)

By answer to interrogatory Sperry then asserted and examined on sixty-two technical items claimed to be trade secrets misappropriated by respondents,—only one of which, the antenna design, proved to be of sufficient substance to survive to trial. Taking a single example, the character of such claims is indicated by the testimony of Sperry's manager, (Joint App. on Appeal, p. A-207)

> Q. And the trade secrets of Sperry are contained in the lorans which have been sold commercially for how long?
> A. 20 to 25 years.
> Q. Are those the same trade secrets to which you refer in this complaint?
> A. Yes.

If respondents did defend against these multiple and abandoned accusations, it can hardly be said that the 'vast amounts of testimony' which petitioner now points to constitute proof of a defense so fraudulent and malicious

as to call for the interposition of extraordinary powers of the Chancellor to oversee the applicable state law. The petition does not describe an 'exceptional' case within the meaning of that term in the citations given, or one which would call for "sanction[s] against a lawless litigant," (Pet. 9).

CONCLUSION

The petition should be dismissed as duplicative. If considered on its merits it should be dismissed as failing either to justify an exercise of this Court's certiorari jurisdiction through a showing of conflict with prior decisions of this Court or as between Circuits, or to factually establish an extraordinary case for equity interposition.

Respectfully submitted,

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